

# CONSTRUCTION

*Pump-priming hopes fade with sovereign outlook downgrade*

**UNDERWEIGHT**

(Maintained)

Joshua Ng

ng-chin-yuing@ambankgroup.com

03-2036 2293

*Rationale for report: Sector update*

## Investment Highlights

- We maintain our **UNDERWEIGHT** recommendation for the construction sector. Given the still elevated national debt and reduced petroleum revenues, we believe the government has very limited room for fiscal manoeuvre, which means that it is unlikely to roll out new public infrastructure projects in a major way over the short term.
- Our view is validated by S&P Global Ratings' downgrade of Malaysia's outlook to negative from stable on 26 June 2020 to reflect a heightened risk of fiscal deterioration, weighed down by the economic impact of the Covid-19 pandemic, depressed oil prices and fiscal stimulus. Nonetheless, the international rating agency affirmed its "A-" long-term and "A-2" short-term foreign currency sovereign credit rating, as well as its "A" long-term and "A-1" short-term local currency ratings on Malaysia.
- Similarly, we do not expect any pick-up in private sector jobs (predominantly property projects) given the acute oversupply situation in the high-rise residential, retail mall and office segments.
- Against this backdrop, the news flow on the local construction sector has largely been negative of late:
  1. Contrary to market speculation, the RM110bil KL-Singapore High Speed Rail (HSR) project has not been revived. Instead, the governments of Malaysia and Singapore have agreed to extend the deferment of the project to 31 Dec 2020, from 31 May 2020;
  2. Contrary to market expectations, the RM21bil MRT3 project has not been included in the newly announced short-term National Economic Recovery Plan (Penjana). Recall, Gamuda has been pitching to the government the idea to earmark the RM21bil project as one of the "anchor" shovel-ready infrastructure projects to revive the economy in the aftermath of the Covid-19 pandemic. Gamuda is confident to hit the ground running in about three months if the project is to be awarded to it directly (vs. 12–18 months if the project is to be awarded via an international tender);
  3. Originally scheduled on 6 Aug 2020, the tabling of the 12<sup>th</sup> Malaysia Plan (which, among others, will earmark mega public infrastructure projects to be implemented in 2021–2025), has been postponed to "a later date", while the tabling of Budget 2021 has been rescheduled to 6 Nov 2020 from 2 Oct 2020; and
  4. While the Chinese main contractor for the RM44bil East Coast Rail Link project has since May 2020 been dishing out subcontracts to local players, these jobs are of: (1) low value, i.e. earthworks and drainage; and (2) smallish in terms of size, i.e. ranging from only RM40mil to RM100mil.
- Meanwhile, there has yet to be any indication from the new government that it will honour the RM2.36bil toll concession disposal deal signed between the previous administration and Gamuda. The proceeds from this deal, if it materializes, could come in handy for Gamuda, if the Penang state government decides to fund the Penang South Reclamation (PSR) component (i.e. the reclamation of three man-made islands with a total area of 4,200 acres at the southern tip of Penang Island) under the Penang Transport Master Plan (PTMP) project via a contractor financing/deferred payment scheme.
- To recap, under the scheme, the appointed contractor for the PSR project is required to come out with RM2.5–3.0bil to fund the reclamation of the 790-acre Smart Industrial Park on the 2,300-acre Island A. Once completed, the state government will sell the industrial park. The cash flow and profit raised from the sale of the industrial park will be used to pay the contractor and also ploughed back to complete the reclamation of Island A, Island B (1,100 acres) and Island C (800 acres), as well as the LRT and Pan Island Link highway under the PTMP project.
- Meanwhile, Sarawak has decided that it wants to take control of its own destiny by resorting to state reserves to fund RM11bil of public infrastructure projects, including the Coastal Road, Second Trunk Road and 11 mega bridges. However, the rollout of work packages from these highly publicised projects seems to have hit a snag after the initial hype.
- We may upgrade our UNDERWEIGHT call on the sector to NEUTRAL/OVERWEIGHT if the government decides to revive key public infrastructure projects, particularly, the KL-Singapore HSR and MRT3, despite the fiscal constraints.
- We do not have any top pick for the sector.

## EXHIBIT 1: VALUATION MATRIX

	Recomm.	Price	FV	Upside	Mkt Cap	FYE	EPS (sen)		EPS growth (%)		P/E (x)		P/B*	ROE*	NDPS*	Div Yield*
		(RM)	(RM)	(%)	(RMmil)		FY20F	FY21F	FY20F	FY21F	FY20F	FY21F	(x)	(%)	(sen)	(%)
Gamuda	UNDERWEIGHT	3.44	2.85	-17.2	8,507.1	Jul	20.9	23.1	-24.5	10.5	16.5	14.9	1.0	7.0	12.0	3.5
IJM Corp#	UNDERWEIGHT	1.80	1.26	-30.0	6,526.3	Mar	8.5	11.2	-20.6	31.8	21.2	16.1	0.6	4.1	6.0	3.3
SunCon	UNDERWEIGHT	1.91	1.18	-38.2	2,469.4	Dec	6.4	11.8	-36.0	84.4	29.8	16.2	4.0	25.1	7.0	3.7
Econpile	UNDERWEIGHT	0.62	0.19	-69.4	829.3	Jun	1.6	2.5	-15.8	56.3	38.8	24.8	1.9	7.9	0.5	0.8
HSL	HOLD	1.08	1.12	3.7	629.3	Dec	6.3	11.2	-33.7	77.8	17.1	9.6	0.7	7.5	2.4	2.2
Kimlun	HOLD	0.72	0.76	5.6	230.8	Dec	7.0	9.5	-56.3	35.7	10.3	7.6	0.3	4.5	3.3	4.6
<b>Weighted Average</b>									<b>-25.0</b>	<b>31.7</b>	<b>20.7</b>	<b>15.6</b>	<b>1.3</b>			

\*FY21 #FY20F and FY21F refer to FY21F and FY22F

Source: AmInvestment Bank

## EXHIBIT 2: MEGA PROJECTS

Project	Value (RM bil)	Status	
		On-going	Pending
KL-Singapore High-Speed Rail	110.0		√
Penang Transport Master Plan	46.0		√
East Coast Rail Link	44.0	√	
MRT2	30.5	√	
MRT3	21.0		√
LRT3	16.6	√	
Pan Borneo Highway, Sarawak	16.5	√	
Pan Borneo Highway, Sabah	12.8		√
Coastal Road, Second Trunk Road and 11 mega bridges in Sarawak	11.0	√	
Central Spine Road	10.7	√	
Sarawak-Sabah Link Road	5.2		√
Klang Valley Double Track (Phase 2)	4.5	√	
Johor Bahru-Singapore Rapid Transit System (JB-Singapore RTS)	3.2		√

Source: AmInvestment Bank, various news reports

**DISCLOSURE AND DISCLAIMER**

This report is prepared for information purposes only and it is issued by AmInvestment Bank Berhad (“AmInvestment”) without regard to your individual financial circumstances and objectives. Nothing in this report shall constitute an offer to sell, warranty, representation, recommendation, legal, accounting or tax advice, solicitation or expression of views to influence any one to buy or sell any real estate, securities, stocks, foreign exchange, futures or investment products. AmInvestment recommends that you evaluate a particular investment or strategy based on your individual circumstances and objectives and/or seek financial, legal or other advice on the appropriateness of the particular investment or strategy.

The information in this report was obtained or derived from sources that AmInvestment believes are reliable and correct at the time of issue. While all reasonable care has been taken to ensure that the stated facts are accurate and views are fair and reasonable, AmInvestment has not independently verified the information and does not warrant or represent that they are accurate, adequate, complete or up-to-date and they should not be relied upon as such. All information included in this report constitute AmInvestment’s views as of this date and are subject to change without notice. Notwithstanding that, AmInvestment has no obligation to update its opinion or information in this report. Facts and views presented in this report may not reflect the views of or information known to other business units of AmInvestment’s affiliates and/or related corporations (collectively, “AmBank Group”).

This report is prepared for the clients of AmBank Group and it cannot be altered, copied, reproduced, distributed or republished for any purpose without AmInvestment’s prior written consent. AmInvestment, AmBank Group and its respective directors, officers, employees and agents (“Relevant Person”) accept no liability whatsoever for any direct, indirect or consequential losses, loss of profits and/or damages arising from the use or reliance of this report and/or further communications given in relation to this report. Any such responsibility is hereby expressly disclaimed.

AmInvestment is not acting as your advisor and does not owe you any fiduciary duties in connection with this report. The Relevant Person may provide services to any company and affiliates of such companies in or related to the securities or products and/or may trade or otherwise effect transactions for their own account or the accounts of their customers which may give rise to real or potential conflicts of interest.

This report is not directed to or intended for distribution or publication outside Malaysia. If you are outside Malaysia, you should have regard to the laws of the jurisdiction in which you are located.

If any provision of this disclosure and disclaimer is held to be invalid in whole or in part, such provision will be deemed not to form part of this disclosure and disclaimer. The validity and enforceability of the remainder of this disclosure and disclaimer will not be affected.